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COMMERCE FOR BEWT/TDAD (STECHSCHULTE)

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SUBJECT: DISCUSSION WITH SOVIET MINISTRY OF FOREIGN TRADE'S MAIN
ADMINISTRATION FOR COMPENSATION AGREEMENTS

SUMMARY: COMOFF AND BEWT /USSR OFFICER BOZEK PAID A VISIT MAY 24
ON A. PONOMAREV, DEP. DIRECTOR OF MAIN ADMINISTRATION FOR COMPENSA-
TION PROJECTS OF USSR MINISTRY OF FOREIGN TRADE. MAIN POINTS RAISED
WITH PONAMAREV BY EMBASSY CALLERS INCLUDED "IDEAL" SCALE OF COM-
PENSATION PROJECTS, CALCULATION OF BUYBACK PRICES FOR COMPENSATION
PROJECTS, AND EXTENT OF QUALITY CONTROL WHICH MIGHT BE PERMITTED TO
U.S. FIRMS IN PROSPECTIVE COMPENSATION PROJECTS. PONOMAREV REPLIED
THAT WHILE IN PRINCIPLE SCALE OF A PARTICULAR COMPENSATION PROJECT
IS NOT LIMITED, IN PRACTICE MEDIUM (\$20 MILLION OR MORE) AND LARGE
(\$100 MILLION AND MORE) COMPENSATION PROJECTS ARE BETTER SUITED TO
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NEEDS AND CAPABILITIES OF USSR AND UNITED STATES. PONOMAREV HELD
THAT BUY-BACK PRICES FOR COMPENSATION PRODUCTS ARE NORMALLY BASED ON
A FORMULA LINKED TO WORLD MARKET PRICES. USUALLY THIS FORMULA DOES
NOT ALLOW FOR DISCOUNTS; HOWEVER, UNDER SPECIAL CIRCUMSTANCE
(E.G., SAKHALIN PROJECT) HE DID ADMIT EXCEPTIONS ARE MADE TO GENERAL
RULE. SINCE PONOMAREV (AND OTHER MFT OFFICIALS IN SEPARATE MEETINGS)
DID NOT CHOOSE TO RESPOND TO QUESTIONS REGARDING AMERICAN QUALITY

CONTROL IN COMPENSATION PROJECTS, IT WOULD SEEM THAT THIS IS STILL A SENSITIVE SUBJECT FOR MFT. END SUMMARY.

1. ON MAY 24 BEWT/USSR OFFICER BOZEK ACCOMPANIED BY COMMOFF PAID A CALL ON MAIN ADMINISTRATION FOR COMPENSATION PROJECTS (MACP) USSR MINISTRY OF FOREIGN TRADE. DEPUTY DIRECTOR OF MACP, ANDREY S. PONOMAREV, AND A MEMBER OF HIS STAFF, TOM (SIC) FEDOROVICH BATURIN, INTRODUCED AS MEMBER OF SOVIET DELEGATION TO THE 6TH JOINT COMMERCIAL COMMISSION, REPLIED TO QUESTIONS ON COMPENSATION PROJECTS (CP) RELATIVE TO SOVIET CONCEPTION OF IDEAL SIZE FOR A CP AND SOVIET METHOD FOR CALCULATING BUY-BACK PRICE OF A COMPENSATION GOOD UNDER THESE ARRANGEMENTS. ALTHOUGH IN PRINCIPLE PONOMAREV THOUGHT THAT CP'S COULD INCLUDE TRANSACTIONS RANGING IN VOLUME FROM \$1 MILLION TO \$20 BILLION, HE SAID THAT MORE CP'S WERE OF MEDIUM AND LARGE-SIZES. AS AN EXAMPLE OF A SMALL CP, HE MENTIONED A CONTRACT OF ABOUT ONE MILLION DOLLARS FOR DELIVERY OF DIES, MOLDS, AND RELATED EQUIPMENT BY UK FIRM, MARX TOYS, IN RETURN FOR DELIVERIES FROM THE USSR OF PLASTIC MOLDED TOY PARTS. PONOMAREV NOTED THAT THIS WAS A UNIQUE TRANSACTION AND ONE WHICH DOES NOT MEET MOST PRESSING ECONOMIC DEVELOPMENT NEEDS OF USSR. HE SAID, HOWEVER, SUCH DEALS WERE POSSIBLE WHEN BUILT ON A BASE OF LARGE-SCALE BILATERAL CP'S. A MEDIUM-SIZE CP, IN PONOMAREV'S OPINION, WOULD BE BENDIX SPARK PLUG EAL, ESTIMATED AT \$25 MILLION. AS EXAMPLES OF LARGE-SCALE CP'S, HE MENTIONED THE \$20 BILLION OXY DEAL, THE \$600 MILLION ICI-DAVY-POWERGAS/KLOECKNER DEAL AND PROSPECTIVE MULTI-BILLION DOLLAR YAKUTSK GAS FIELD DEAL. (ON LATTER DEAL, HE SAID THAT ONLY 300 BILLION CUBIC METERS OF GAS RESERVES NEED YET TO BE PROVED IN ORDER TO REACH COMMERCIALLY VIABLE LEVEL OF ONE TRILLION CUBIC METERS.)

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2. ON WHOLE, PONOMAREV REPEATED OFT-EXPRESSED SOVIET VIEW THAT CP(S) WITH U.S. SHOULD BE LARGER THAN THOSE WITH WESTERN EUROPEAN COUNTRIES AND JAPAN, SINCE U.S. CAN BETTER MEET LARGE-SCALE NEEDS OF USSR AND CAN BETTER ABSORB RESULTANT PRODUCT OF CP'S. HE NOTED, HOWEVER, THAT U.S. FIRMS COULD NOT EXPECT TO SIGN ANY SIGNIFICANT CP'S UNTIL "OBJECTIVE CONDITIONS" (FOR TRADE) WERE MORE FAVORABLE INCLUDING AVAILABILITY OF U.S. GOVERNMENT FINANCING.

3. PONOMAREV NOTED THAT THE BRITISH OFFER OF FINANCING (WILSON CREDIT) WAS BEING USED AND CP'S COULD PROVIDE AVENUE FOR FULL UTILIZATION OF CREDIT LINE. AS AN ASIDE, HE SAID THAT SMALL COUNTRIES SUCH AS HOLLAND COULD NOT PROVIDE SUFFICIENT FINANCING OR EQUIPMENT ON A LARGE ENOUGH SCALE TO SATISFY NEEDS OF USSR.

4. IN DISCUSSING CALCULATION OF BUY-BACK PRICES FOR GOODS RESULTING FROM A CP, PONOMAREV CLAIMED THAT THEY WERE BASED ON A FORMULA LINKED TO WORLD MARKET PRICES OVER A MUTUALLY AGREED (BETWEEN USSR AND WESTERN FIRM) PERIOD. PRICE DATA BASE IS NORMALLY CHANGED EVERY 6-12 MONTHS WITH 12 MONTH PERIOD BEING MOST TYPICAL. PONOMAREV FIRMLY

MAINTAINED THAT NO DISCOUNTS WERE GIVEN; BUT HE DID SAY THAT, UNDER SPECIAL CIRCUMSTANCES, SOME EXCEPTIONS TO BAN ON DISCOUNT POLICY WERE PERMITTED. HE CITED SAKHALIN PROJECT WHERE JAPANESE COMPANIES AND GULF OIL HAD PROVIDED RISK CAPITAL FOR DEVELOPMENT OF OFFSHORE OIL AND GAS AS A PROJECT IN WHICH A DISCOUNT WOULD BE GIVEN.

5. ALTHOUGH QUESTION OF QUALITY CONTROL WAS BROACHED SEVERAL TIMES, PONOMAREV REFUSED TO ADDRESS HIMSELF TO ISSUE. IN SEPARATE MEETINGS WITH OTHER MFT OFFICIALS--NABOROV OF NIKI, AND TRETYUKHIN OF THE PLLFN SG-ECONOMIC ADMINISTRATION--QUESTION OF QUALITY CONTROL WAS SIMILARLY SIDE-STEPPED BY SOVIET OFFICIALS. (COMMENT: IT WOULD SEEM THAT A POLICY ON QUALITY CONTROL HAS NOT YET BEEN FORMULATED AND MFT OFFICIALS ARE THEREFORE RELUCTANT TO DISCUSS THIS ISSUE UNTIL FIRM POLICY LINE HAS BEEN PROMULGATED WITHIN USSR GOVERNMENT. IT IS CLEAR FROM PONOMAREV'S STATEMENTS--AS WELL AS STATEMENTS OF OTHER MFT OFFICIALS-- THAT WHEN MFT CONTEMPLATES A CP, DOLLAR VALUES INVOLVED BEGIN IN TENS OF MILLIONS OF DOLLARS, THUS MAKING IT LIMITED OFFICIAL USE

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UNLIKELY THAT WE WILL SOON SEE MANY CP'S SUCCESSFULLY NEGOTIATED BY U.S. FIRMS WITH SOVIETS IN ABSENCE OF LOWER FINANCING COSTS THAT COULD COME FROM USG-BACKED CREDITS.).
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